STATE OF NORTH DAKOTA
OFFICE OF STATE TAX COMMISSIONER
RYAN RAUSCHENBERGER, COMMISSIONER

# Memorandum

**To:** Oil and Gas Producers and Purchasers

**From:** North Dakota Tax Commissioner's Office

**Date:** October 1, 2015

**Subject:** 2015 Legislative Changes to Oil Extraction Tax

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Two major pieces of legislation relative to oil and gas taxation were enacted by the 64th North Dakota Legislative Assembly.

**House Bill 1476**

HB 1476 repeals the old "small" and "big" trigger methods and eliminates most of the oil extraction tax exemptions and rate reductions. Beginning January 1, 2016, the oil extraction tax rate will be reduced from 6.5% to 5% and a new "high price" trigger method is created that raises the oil extraction tax rate to 6% in a triggered-on environment. The final version of this bill, signed by the Governor, is available on the Secretary of State's website at http://sos.nd.gov/files/legislation/1476.pdf.

**Senate Bill 2015**

SB 2015 corrects changes made in HB1476 relating to tertiary recovery incentives for qualifying units with production in the Bakken or Three Forks formations. The final version of this bill, signed by the Governor, is available on the Secretary of State website at http://sos.nd.gov/files/legislation/2015.pdf.

**Legislative Change Highlights from HB1476 and SB2015**

Reduction of the oil extraction tax from 6.5% to 5%

- Beginning January 1, 2016, all oil production will be subject to a 5% oil extraction tax rate unless the production has qualified for one of the surviving exemption or rate reduction incentives.

Current price triggers will be eliminated effective December 1, 2015, and January 1, 2016.

A new "high price" trigger is created to raise the oil extraction tax rate to 6% when the average monthly oil price exceeds the trigger price for three months straight. Subsequently, the rate lowers back to 5% when the average monthly oil price is below the trigger price for three months straight.

- New trigger price of $90
- Average price measured as the monthly average daily closing price for a barrel of west Texas Intermediate Cushing crude oil, as those prices appear in the Wall Street Journal (weekends and holidays must be included utilizing the previous daily closing price)
- Trigger period of three consecutive months with an average price above or below the trigger price

The Tax Commissioner has added new oil well codes to facilitate the tax rate changes noted above:

- Active 5% oil extraction tax rate – well code T5
- Active 6% oil extraction tax rate – well code T6

Elimination of oil extraction tax exemptions and rate reductions:

- Exemptions and rate reductions that expire for production occurring after November 30, 2015.
    - New horizontal well 24 month exemption, well code HE
    - New well reduced 4% tax rate - NW well code
- Exemptions and rate reductions that expire for production occurring after December 31, 2015:
    - New vertical well 15 month exemption – EN well code
    - "Small trigger" Horizontal New Well reduced 2% tax rate – HN well code
    - Horizontal reentry well 9 month exemption – HR well code
    - Inactive well 10 year exemption – IE well code
    - Workover well 12 month exemption – WP well code
    - Workover reduced 4% tax rate – W4 well code
    - Indian land 60 month exemption – FE well code
    - Secondary recovery reduced 4% tax rate – SR well code
    - Tertiary recovery reduced 4% tax rate – TR well code
    - Enhanced recovery reduced 4% tax rate – R2 well code

Retention of oil extraction tax exemptions and rate reductions:

- Exemptions
    - Stripper wells – S1, S2, S3 and S4 well codes
    - Incremental production from qualifying secondary or tertiary recovery units for a period of five or ten years – R1 well code
- Rate Reductions
    - Non-Bakken/Three Forks reduced 2% tax rate – RN well code

Changes to retained oil extraction tax exemptions:

- Exemption for incremental production from a qualifying tertiary recovery unit
    - The lifetime oil extraction tax exemption on incremental oil produced from a qualifying project utilizing $CO_2$ was eliminated
    - The ten year exemption on incremental oil was limited on qualifying projects in the Bakken and Three Forks formations
        - The incentive starting period was suspended until July 1, 2017, on any incremental production from a horizontal well in a qualified tertiary recovery unit
        - The incentive period was restricted to five years on incremental production from a horizontal well in a qualified tertiary recovery unit

Tax Commissioner's note on inventory considerations relating to tax and incentive rate changes:

- Crude oil is taxed at the rate in effect at the time of production. Inventory must be accounted for on a first-in-first-out basis for tax purposes. Sales of inventory that has been produced when different tax rates were in effect requires multiple entries on the monthly report to account for the volumes at the different tax rates.

For specific information regarding legislative changes to the oil extraction taxes, please refer to North Dakota Century Code § 57-51.1 (www.legis.nd.gov/cencode/t57c51-1.pdf).

Contact our office at 701.328.3657 or ***oiltax@nd.gov*** if you have any questions.